Case Study

Marco Bertini is an assistant professor of marketing at London Business School. **Nirmalya Kumar** is a professor of marketing and codirector of the Aditya Birla India Centre at London Business School.

The Experts

Georg Tacke is the co-CEO of Simon-Kucher & Partners. He is based in Bonn, Germany.

Anne Gro Gulla is the group branding director for Telenor Group in Oslo, Norway.

HBR's fictional cases present dilemmas faced by real leaders and offer solutions from experts.

ILLUSTRATION: ELLIE FOREMAN-PECKZ

What do you do when one of your small competitors pulls out its big gun?

by Marco Bertini and Nirmalya Kumar

The Upstart's Assault

Joseph Ulan spent his first few minutes in the office on Wednesday Googling the weather in Sardinia. He, Ana, and the boys were set to fly there on Saturday, and although he wasn't looking forward to the Alitalia flight, the prospect of two weeks on the beach seemed heavenly. No questions from his CEO about why the new customer initiatives were behind schedule. No excuses from the landline, mobile, and broadband division heads about why their respective service centers and billing systems couldn't be integrated. No meetings to run, no presentations to prepare. He couldn't wait to step out of his chief marketing officer suit and into his Daddy sandals and swim trunks.

Only 72 more hours, Joe thought, smiling as he opened that morning's *Financial Times*. But the ad spanning page 3 made his lips narrow. "Free broadband forever with TelZip! Save at least €450 a year when you switch from Meridicom!"

TelZip, a small mobile-network operator eager to break into new markets, had decided to offer free broadband service to business customers who were willing to leave their current provider and enter into a long-term contract. As the oldest and largest telecommunications player in the country, Meridicom was accustomed to seeing both old and new competitors—bigger mobile companies, cable TV operators, and internet providers—undercut its prices on all types of services by the usual 10%. Meridicom was the industry price leader, so when it published rates, everyone else reacted predictably. But TelZip was now changing the game—not only giving away a high-growth, high-margin product but attacking Meridicom head-on.

Joe had barely digested the news when CEO Gerald Segner opened the door. “Why didn’t we know about this?” he asked, stern but calm.

“We suspected that TelZip was planning to go after new markets,” Joe answered. “But I must admit I didn’t expect it to be broadband—or for them to give it away free for life.”

“Look, the ad is a shock, but it’s not really TelZip I’m worried about,” Segner said. “We’ve ignored price attacks from gnats like these in the past, and we always come out on top. Meridicom is one of the best-known brands in this country, in Europe even—and customers, especially business customers, know and trust our quality. We don’t want to jeopardize that. But the real question is: Could this threat become bigger? The word ‘free’ gets attention, especially from the press. If our larger competitors follow suit, would customers then take the offer more seriously?”

“It’s a good question.”

“Don’t forget, this isn’t only free broadband,” Segner continued. “If customers decide to migrate to TelZip, we’ll lose their landline revenue and, worse, the connection between the local exchange and their home or office. That’s the umbilical cord—it’s how we gather data about customers and figure out how to build and sell them tomorrow’s telecom services.”

> “Do you really think people will renew their contracts with us out of nostalgia?”

Joe nodded. He may have been new to the business, but he understood the importance of owning the “last mile” in the network.

“This is just the sort of thing I brought you over from Pimmit for,” Segner said. “You picked the right fights there, internally and externally. You got the division heads to work together and even built market share with all those newbies nipping at your heels. And you did it without hurting the brand. I’m sure you can do it again here.”

Heels Dug In

An hour later Joe and the Meridicom division heads—Adam Dupree at Landline, Emeline Ricard at Broadband, and Frank Lopez at Mobile—were sitting around a table in the executive dining room. Even on normal days these meetings were contentious, so Joe had decided to bring everyone up to the 12th floor and order pastries, coffee, and tea. Harder to shout with food in your mouth, he figured.

“I’ve been in this business longer than both of you, and I can tell you it’ll blow over,” Adam said, pouring coffee into a porcelain cup but ignoring the overflowing basket of buns. “First, it’s almost August and the entire country is about to shut down. No one is going to make a serious business decision now. Second, TelZip isn’t offering anything for free. You have to pay for the landline service. Customers are not stupid. And even the discount doesn’t really matter. Our business customers emphasize price in focus groups and on questionnaires. But when it comes down to it, choosing a communications provider is about trade-offs, and they care most about quality and convenience. We have an 85% market share in landline, compared with TelZip’s 5%. Would you trust them with your conference calls? And you know how much businesses—even individuals—hate the hassle of switching landline providers.”

“Yes, but you can’t say Meridicom is convenient for our customers. If anything, we complicate their lives,” Joe countered, masking his exasperation. “When businesses use us for all three services, we send them three bills! When they have questions, we have them talk to call centers in three different countries. Do you really think people will renew their contracts with us out of nostalgia?”

“Don’t even think about offering our service for nothing,” Emeline said. “TelZip can do it because their broadband business is brand-new. We have a 60% market share, and we’re contributing 25% to the top line right now. We’re also the fastest-growing part of this company, and we have the highest margins. So you can’t kill us off. If Meridicom is going to offer discounts, all the product lines need to take the pain.”

“We shouldn’t discount at all,” Adam said. “But if we do, it’s certainly not coming out of our business. We’re number one in our market, 70% of Meridicom’s revenues. Why should we cut prices?”

That was the trouble. Segner wanted to end this bickering and focus all the units on improving the customer experience. He had been frustrated by his own lack of progress for six months and then brought Joe in to help. In theory, the division heads should agree to their CEO’s strategy. But

“Can my own tweets be used against me?”

CARTOON: ROY DELGADO

Tell us what you'd do if you were in Joe's shoes.
Go to **hbr.org**.

when it came down to it, they cared more about protecting their turf than working together. They were quasi-independent operators, still remunerated based on the performance of their own units. And because all three continued to make money for the company, it would be hard to move them away from the status quo.

Frank had been quietly sipping tea and taking notes in his Moleskine. Adam and Emeline, whose divisions were several times the size of his, called him "the doodler" behind his back. But Joe considered him to be the most thoughtful of the three.

"Adam," Frank said, "I think you're ignoring that TelZip is a serious player in the mobile phone market now. They have a 25% share, compared with our 5%, and a lot of name recognition. The only way we're going to catch up to them and others in that business is by offering something more compelling. Sure, customers care about both service and price, especially nowadays. But they also want predictability about what their costs will be each month, and mobile is the biggest and most variable component of that. Broadband is less of a worry because it's a fixed charge. Still, if you're looking for reliable rates, 'free forever' is about as good as it gets."

Joe sighed. Yes, free forever was pretty hard to beat.

Fire and Wine

Joe was standing outside the little wine shop around the corner from his office, trying to remember whether his wife wanted red or white for the dinner party that night, when he heard a shout from behind him.

"Joe, I'm so glad I ran into you." It was Charles DeGraff, Meridicom's head of sales. "Has this TelZip thing driven you to drink?"

"It's been rough. But, no, my wife asked me to pick up some wine, and I know this guy always ducks out before 7."

"You should try the one down the street—open until 11 and 10% off when you buy six bottles. Anyway, while I have you, I want to say that this TelZip thing is a huge opportunity for us. We should match them—full-page ad in tomorrow's FT. Show all these little guys who's boss. Sure, margins might suffer for a while. But we'll kill everyone else off and keep—even boost—our market share."

"You really think we should fight fire with fire?"

"Look, all I hear from our major business customers is that we're too expensive. They tell me: 'How can we run a successful company when we're paying so much to you?' Segner wants us to focus on the customer, right? Well, the customer wants us to acknowledge the competition in our market and give them a better deal."

Sit Tight or Stand Up?

Joe had missed his kids' bedtime and was on track to be late with the wine for the dinner party when Segner stopped by on his way out of the building. "Just checking in about TelZip. What's the plan?"

The truth was Joe hadn't decided. Doing nothing, as Adam had advised, might make sense. TelZip wasn't a large competitor, and Segner cared more about pricing power and margins than about small dips in market share. But perhaps Charles was right to advocate for a direct response. Meridicom was large enough to make "free forever" credible, maybe even turn this challenge into an opportunity. The question was how—and, given the difficulty Joe had already faced in getting the divisions to work together, how quickly.

Should Joe ignore or respond to TelZip's bold move?

See commentaries on the next page.

The Experts Respond

Georg Tacke, co-CEO of Simon-Kucher & Partners

DURING MY 20 years of telecommunications consulting, I have often seen situations like Joe's, although the competitive attack on his company is particularly severe. Meridicom's lack of a reaction plan and the posturing of its division heads also sound familiar to me.

The attack by TelZip typifies those of challengers that want to intrude into new business areas. They choose a battlefield where they can really hurt the incumbent without exposing themselves to much cannibalization. In this case, TelZip pulls out the big gun on broadband: "free for life." But that's only one service; its customers still must pay for mobile and landline.

In my experience, simply matching a small competitor's prices is the worst reaction. A "price war" signal is sent out to other players, and profits go down the drain. Attackers rarely withdraw, and often a takeover keeps them alive. An incumbent that matches prices from all comers will eventually give everything away for free.

Simply matching a small competitor's prices is the worst reaction.

Doing nothing can be a valid strategy. In this case, however, action is needed. TelZip has a substantial presence in the mobile market, and Meridicom has issues unrelated to the attack to resolve. There is no patent remedy for Joe, but the following principles could help him construct a viable plan of action:

1. Don't limit your response to the product area that's under attack. Instead, open another battlefield that has a lower risk of cannibalization. For example, Meridicom could fight back on mobile services, where it has only a 5% market share, and put TelZip on the defensive.

2. Consider not only price level but also price model reactions. Such a move may meet customer needs without putting profits at such high risk. Swisscom, for example, switched its model from pay per minute to pay per call—and thereby defended its dominant market position in Switzerland.

3. Take advantage of your portfolio breadth. Design attractive bundles and develop smart discount models to retain customers and maximize your share of their wallets. That's especially effective with B2B customers, as list prices and single price points are less important for them than for individual consumers.

Unfortunately, Meridicom still has the silo-like, tech-focused mind-set of the old "telco industry." Modern, customer-centric organizations such as Swisscom, Optus, and Deutsche Telekom (former clients of my firm) can tackle challenges more flexibly, using approaches such as product integration, overall invoicing, single points of contact, and aligned loyalty programs. Meridicom needs to behave more like those companies.

Anne Gro Gulla, group branding director for Telenor Group

I SYMPATHIZE with Charles, the sales director, whose gut advice is to "fight fire with fire." But how smart is that?

As the sixth-biggest mobile operator in the world (as measured by subscribers) and with leading positions in our 13 markets, Telenor frequently faces these issues.

Continued dominance means under-standing and responding to customer

WHAT WOULD YOU DO? SOME ADVICE FROM OUR READERS

Joe should consider a possible ad campaign that would spread fear, uncertainty, and doubt about "free" broadband and that would position Meridicom as a reliable partner. But the real work is longer-term, strategic, and structural.
Neil LaChapelle, *learning development specialist, The Co-operators, Ontario, Canada*

If the customers who drive Meridicom's profitability want a technology partner that helps them be ready for anything, answering TelZip's challenge would be a poor investment. An integrated customer expe-rience is what's needed—and something TelZip can't match.
Linda Ireland, *partner, Aveus, St. Paul, Minnesota*

Perhaps the smartest way that Meridicom could hit back at TelZip would be to bundle all its services—landline, broadband, and mobile—for busi-ness customers at a nice discount. To receive the special pricing, partici-pants would have to sign a long-term deal.
Greg Howard, *marketing consultant, St. Louis*

Meridicom should make a frontal attack on the mobile market. Broad-band and landline should generate enough revenue to keep the company profitable while matching or undercutting TelZip's wireless prices.
Ben Hoffman, *graduate student, North Dakota State University*

HBR's case studies appear at **hbr.org** prior to publication here.

It's better to keep all the cannibals in the family.

needs. Subscribers are loyal only until a better offer comes along. If price is the main reason customers want to change their supplier, then Meridicom has not built real value into its offering.

The company's brand may stand for trust and quality, but customers who still receive bills from three different divisions clearly deserve better. That kind of change doesn't happen overnight and requires involvement across the entire company. However, once it is achieved, competitors cannot easily copy it.

So what should Joe do before his vacation? Well, he should not engage in a price war by immediately placing an ad in the *Financial Times*, as Charles suggests. A matching "free" offer would erode not only Meridicom's margins but also those of the entire industry in that market segment. However, Joe must ensure that all customer-facing employees have good answers at their fingertips about why it's worth sticking with Meridicom. He could also develop an ad that focuses on the quality of the brand.

More important, the moment Joe returns from vacation, he should start remaking the company as a champion of its customers. He must give the division heads an incentive to work together and create more value in Meridicom's offerings across the board. It might be that the pricing strategy needs to change. In several of Telenor's markets we have fighter brands that target very price-sensitive services; these include Talkmore and Glocalnet, our respective mobile offerings in Norway and Sweden. These offshoots might take share from the mother brand, but we think it's better to keep all the cannibals in the family than to be eaten alive by strangers.

In the end Joe might be grateful that TelZip was a catalyst for change at Meridicom. ⛉

HBR Reprint R1007R
Reprint Case only R1007X
Reprint Commentary only R1007Z